

MICHIGAN ECONOMIC OUTLOOK AND HOUSE FISCAL AGENCY REVENUE ESTIMATES



**FISCAL YEARS
1999-2000 AND 2000-01**



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FOREWORD

The House Fiscal Agency (HFA) is pleased to present this report to members of the Michigan House of Representatives. The purpose of the report is to inform members about the revised House Fiscal Agency General Fund/General Purpose and School Aid Fund revenue estimates for fiscal year (FY) 1999-2000 and FY 2000-01. The estimates reported herein will be presented to the Consensus Revenue Estimating Conference on May 19, 2000, and will be used to facilitate the consensus estimating process.

Included are HFA analyses of important factors that will affect the state and national economies through the year 2001, estimates of state compliance with the Constitutional State Revenue Limit, and year-end balance estimates for General Fund/General Purpose, the School Aid Fund, and the Countercyclical Budget Stabilization Fund.

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EXECUTIVE SUMMARY

Michigan continued to experience robust economic growth throughout Fiscal Year (FY) 1998-99 and the first half of FY 1999-2000. Baseline General Fund/General Purpose (GF/GP) revenues and School Aid Fund (SAF) revenues grew 9.2% and 5.9%, respectively, in FY 1998-99. Baseline figures do not include the effects of tax policy changes. Michigan's unemployment rate averaged 3.8% in 1999, remaining below the national average rate of 4.2%, and inflation in the U.S. was under control at 2.2%.

The House Fiscal Agency (HFA) expects the current economic expansion to continue through FY 2000-01, but the rate of growth will begin to slow in the next several months. The current expansion is already the longest expansion on record. The most important aspects of the HFA forecast are summarized in the following.

U. S. Forecast

Real GDP growth will increase from 4.2% in Calendar Year (CY) 1999 to 4.7% in CY 2000 before declining to 3.5% in CY 2001.

Inflation will increase from 2.2% in CY 1999 to 2.6% in CY 2000, and then drop to 2.1% in CY 2001.

Light vehicle sales were 16.8 million units in CY 1999, and will increase to 17.2 million units in CY 2000 before dropping to 16.6 million units in CY 2001.

The *national unemployment rate*, which was 4.2% in 1999, is expected to drop slightly to 4.1% in CY 2000, and remain at

that level in CY 2001.

Interest rates on three-month T-bills averaged 4.6% in CY 1999, and should jump to 6.0% in CY 2000, and 6.2% in CY 2001.

Michigan Forecast

Michigan personal income increased by 4.5% in CY 1999. The rate of growth will increase to 5.5% in CY 2000 before falling to 5.0% in CY 2001.

Michigan unemployment rates will drop from 3.8% in CY 1999 to 3.7% in CY 2000 and 3.5% in CY 2001.

Inflation, as measured by the Detroit Consumer Price Index, will rise from 2.6% in CY 1999 to 2.8% in CY 2000, and then drop to 2.4% in CY 2001.

U State Revenues

Total baseline GF/GP and SAF revenues were \$18.9 billion in FY 1998-99, and will increase 5.7%, to \$20.0 billion, in FY 1999-2000 and 4.4%, to \$20.8 billion, in FY 2000-01. Baseline revenues do not include prior-year fund balances or reflect the effects of recent tax policy changes.

U State Revenue Limit

Total state revenues were above the state revenue limit by \$21.7 million in FY 1998-99 and are expected to be under the limit by \$41.2 million in FY 1999-2000, and \$434.5 million in FY 2000-01.

U Year-End Fund Balances

The *year-end GF/GP balance* was \$0 in FY 1998-99 and is expected to be \$100.4 million in FY 1999-2000.

The *School Aid Fund year-end balance* was \$572.8 million in FY 1998-99, and is expected to be \$989.2 million in FY 1999-2000.

The *Countercyclical Budget Stabilization Fund year-end balance* was \$1,222.5

million in FY 1998-99, and is expected to be \$1,305.6 million in FY 1999-2000.

U Baseline and Actual Revenue Estimates

Table 1 reports GF/GP and SAF revenues in terms of baseline and actual revenues (any discrepancy in total amount is due to rounding).

Baseline revenues do not include the impact of partial-year policy changes or certain policy changes that have only recently occurred.

Baseline estimates are comparable across fiscal years and demonstrate the changes to state revenues that are driven by changes in the economy.

Actual GF/GP revenues capture the effects of all policy changes and represent resources actually available.

Actual SAF revenues for FYs 1998-99, 1999-2000, and 2000-01 do not include transfers from the BSF of \$212.0 million, \$73.7 million, and \$32.0 million, respectively, pursuant to 1997 PA 144. Actual SAF revenues do not include transfers from GF/GP or beginning fund balances.

Table 1

| HFA REVENUE ESTIMATES (Millions of Dollars) | | | |
|---|---------------------|-------------------|-------------------|
| | Final FY 1998-99 | FY 1999-2000 | FY 2000-01 |
| <u>BASELINE</u> | | | |
| GF/GP | \$9,573.8 | \$10,040.1 | \$10,503.0 |
| SAF | <u>9,314.4</u> | <u>9,925.2</u> | <u>10,341.6</u> |
| TOTAL | \$18,888.2 | \$19,965.3 | \$20,844.6 |
| <u>ACTUAL</u> | | | |
| GF/GP | \$9,462.7 | \$9,656.1 | \$9,778.0 |

| | | | |
|--------------|-------------------|-------------------|-------------------|
| SAF | 9,309.9 | 9,936.9 | 10,365.3 |
| TOTAL | \$18,772.6 | \$19,593.0 | \$20,143.3 |

ECONOMIC ASSUMPTIONS AND FORECASTS

This section discusses the economic assumptions used by the House Fiscal Agency to produce its updated revenue forecasts for FY 1999-2000 and FY 2000-01.

U U.S. Forecast

There was a higher-than-expected federal budget surplus in 1998. The 1998 surplus reached \$69.2 billion on a unified budget basis — a \$91 billion improvement over 1997. Current estimates suggest the federal budget surplus will exceed \$120 billion in 1999 and climb to almost \$180 billion in 2000. While a small portion of the improvement was due to smaller-than-projected increases in spending on defense and transfer payments to individuals, most of the surplus was due to higher-than-anticipated increases in personal tax payments. Moderate interest rates have also helped to hold down federal government interest payments.

Total federal current expenditures increased 4.9% in FY 1998-99, and are expected to increase by 3.9% in FY 1999-2000 and 3.5% in FY 2000-01.

Non-defense consumption expenditures increased at a 7.4% rate in FY 1998-99 and are expected to increase by 6.6% in FY 1999-2000 and 3.8% in FY 2000-01.

Defense expenditures are expected to increase 3.6% in FY 1999-2000 and 2.4% in FY 2000-01.

The rate of growth of *total federal transfer payments to individuals* is expected to be 3.8% in FY 1999-2000 and 4.9% in FY 2000-01.

The rate of growth in *federal grants-in-aid to state and local governments* is expected to be 7.1% in FY 1999-2000 and 6.1% in

FY 2000-01.

Federal receipts are

expected to increase 6.8% in FY 1999-2000 and 4.2% in FY 2000-01.

SHORT TERM INTEREST RATES

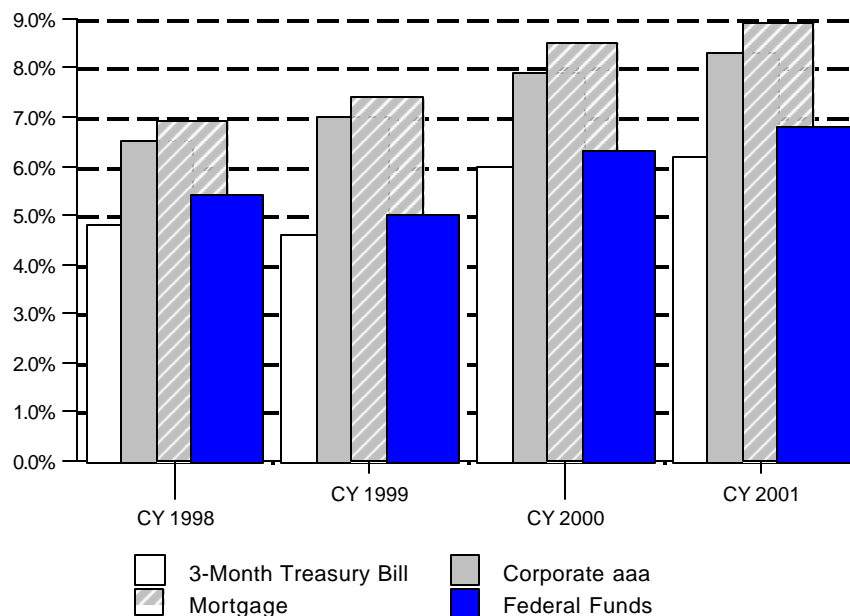


Figure 1

U Interest Rates

Concern about potential inflation has been a prominent theme among economists over the past two years in response to unusually strong growth in real GDP. The U.S. economy, which continues to expand, grew at an annualized real rate of 5.4% in the first quarter of 2000 after posting a 4.2% real growth rate for all of 1999. In an attempt to ward off inflationary forces, the Fed increased the federal funds rate by 25 basis points in both February and March of this year. In spite of these increases, personal consumption expenditures surged at an 8.3% annualized real growth rate in the first quarter of 2000.

The economy is expected to continue to grow throughout FY 1999-2000, and then

slow down a bit in FY 2000-01. Because unemployment continues to hover at historic lows, there is some concern that labor market constraints might exert upward pressures on prices, leading to speculation that the Fed will raise interest rates again in mid-May as well as later on this summer.

The *federal funds rate* is expected to increase from an average of 5.0% in CY 1999 to 6.3% in CY 2000, and reach 6.8% in CY 2001.

The *three-month Treasury bill rate* is forecast to average 6.0% in CY 2000 and 6.2% in CY 2001.

The *30-year Treasury bond rate* is expected

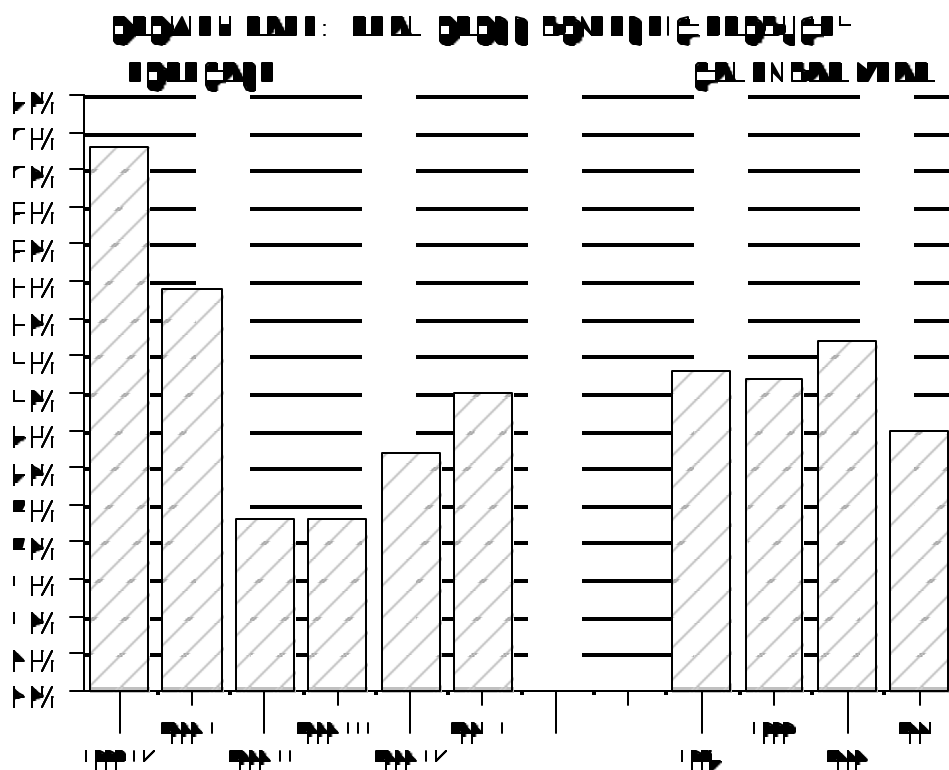
to climb from an average of 5.9% in CY 1999 to 6.5% in CY 2000, and to 7.0% in CY 2001.

Conventional mortgage rates are expected to increase from 7.4% in CY 1999 to 8.5%

in CY 2000 and 8.9% in CY 2001.

Corporate aaa rates are expected to increase from 7.0% in CY 1999 to 7.9% in CY 2000 and 8.3% in CY 2001.

Figure 2



*Seasonally Adjusted Annual Rate (SAAR)

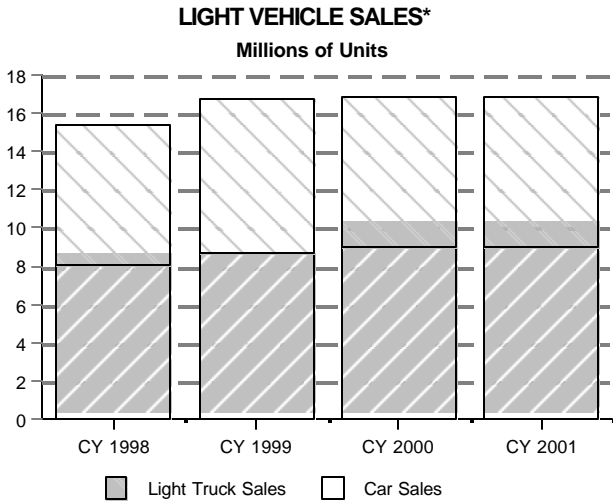
U Real GDP

The economy, continuing its robust performance, grew at a rate of 4.2% during CY 1999, fueled by an annualized fourth quarter growth rate of 7.3%. The growth rate for the first quarter of CY 2000 was 5.4%; growth rates are expected to be somewhat lower than this during the remainder of the forecast period. Calendar year 1999 also witnessed the rebound of many Asian and European economies. This should promote increased U.S. exports and contribute to economic growth for CYs 2000 and 2001.

Also contributing to the high growth rate is robust private consumption. Personal consumption during the first quarter of CY 2000 surged at an annualized real growth rate of 8.3%, outstripping all expectations. Households, encouraged by rising stock prices and increasing home values, are feeling wealthier and thus spending more. Barring a major and prolonged correction, this phenomenon should continue throughout the forecast horizon, albeit at a less vigorous pace.

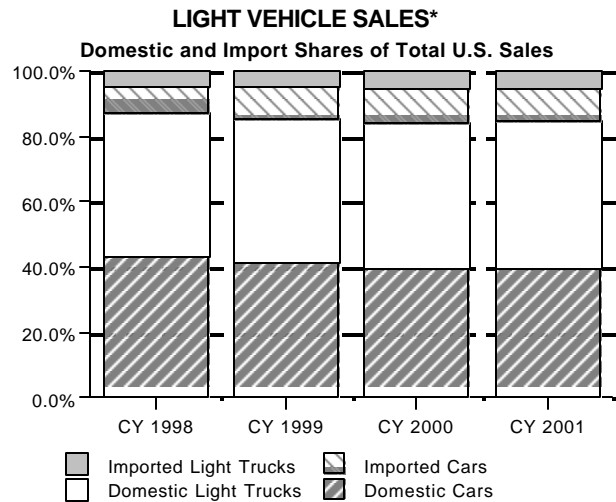
Real GDP increased by 4.2% in CY 1999, and is expected to grow 4.7% in CY 2000 and 3.5% in CY 2001.

Figure 3



*Seasonally Adjusted Annual Rate (SAAR)

Figure 4



U Light Vehicle Sales

Sales of light vehicles set an all-time high in CY 1999, eclipsing the previous record of 16.3 million units set in CY 1986. This trend is expected to continue through CY 2000 before slowing down somewhat in CY 2001. *Light vehicle sales* are anticipated to rise from 16.8 million units in CY 1999 to 17.2 million units in CY 2000, and then drop to 16.6 million units in CY 2001.

Over the past several years there has been a shift in sales away from cars and toward light trucks. This is expected to slowly continue; by the end of the forecast period, light vehicle sales will be split almost evenly between cars and light trucks. *Light trucks* accounted for approximately 48.1% of light vehicle sales in CY 1999 and are expected to account for 48.5% percent of total sales in CY

2000 and 48.9% in CY 2001.

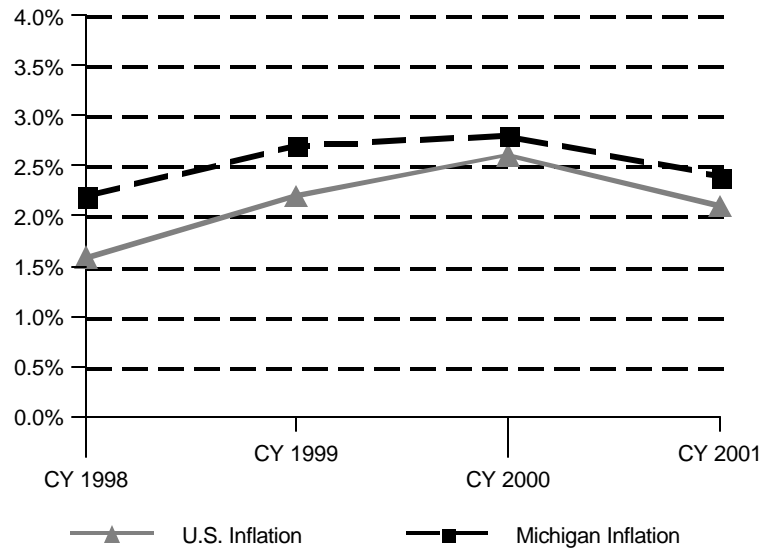
U Import Share of Auto Sales

The import share of the automobile market jumped from 17.0% in CY 1998 to 19.8% in CY 1999. The foreign share of car sales is expected to rise to 21.9% in CY 2000 before dropping off to 21.3% in CY 2001. The import share of light trucks is expected to follow a similar pattern as the *import share* rises from 9.4% in CY 1999 to 9.8% in CY 2000 before falling to 9.6% in CY 2001.

When these two impacts are combined, the net result is that the *import share of total light vehicle sales* will rise to 16.1% of the overall market in CY 2000, and then decline to 15.5% in CY 2001.

Figure 5

INFLATION*



*Not Seasonally Adjusted (NSA)

U Inflation: U.S.

Inflation is typically triggered when producers attempt to exceed short-term capacity constraints in the economy and/or when input prices rise. Excess capacity coupled with continued growth in industrial production should help keep inflationary pressures low despite some indications that input prices (such as oil prices, wages, and import prices) may be beginning to rise. Inflation is expected to remain low by historical standards, although it will increase somewhat during CY 2000.

Spot crude oil prices increased significantly during the latter half of CY 1999. The price of benchmark West Texas intermediate crude, which averaged about \$14 per barrel in CY 1998 and \$19.16 in CY 1999, has jumped to \$28.84 per barrel during the first quarter of CY 2000. It is anticipated that oil prices will moderate to

about \$25 per barrel during CY 2000 and \$22 per barrel by the end of CY2001.

The *rate of inflation in core industrial prices*, as measured by the private non-farm output deflator, is expected to increase by approximately 2.1% in CY 2000 and 2.0% in CY 2001.

These factors are expected to lead to an average annual increase in the *U.S. Consumer Price Index-Urban* (CPI-U) of 2.2% in CY 1999, 2.6% in CY 2000, and 2.1% in CY 2001.

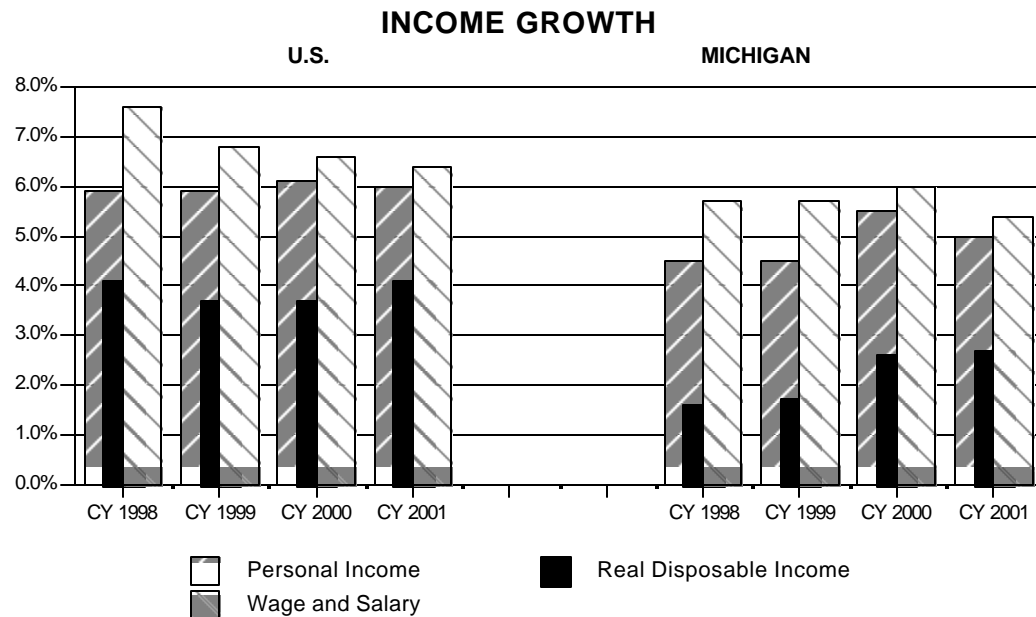
U Inflation: Michigan

The cost of living in Michigan, as measured by the *Detroit Consumer Price Index for Urban Consumers* (Detroit CPI-U), increased by 2.7% in CY 1999 — modestly higher than the national average. With the exception of 1994 and 1995 figures which were skewed due to the increase in the

sales tax rate, inflation since 1991 has been at or below 2.8% each year.

Inflation in Michigan is expected to rise by 2.8% in CY 2000 and 2.4% in CY 2001.

Figure 6



U Income Growth: U.S.

Total *U.S. personal income* grew at a 5.9% rate in CY 1999. Personal income growth is expected to rise to 6.1% in CY 2000 before dropping slightly to 6.0% in CY 2001.

U.S. wage and salary income growth (6.8% in CY 1999) is expected to slow down slightly, but still grow at a faster rate than total personal income. It is anticipated that wage and salary income growth will decline to 6.6% in CY 2000 and fall to 6.4% in CY 2001.

Moderate growth in inflation resulted in a 3.7% rate of growth of *U.S. real*

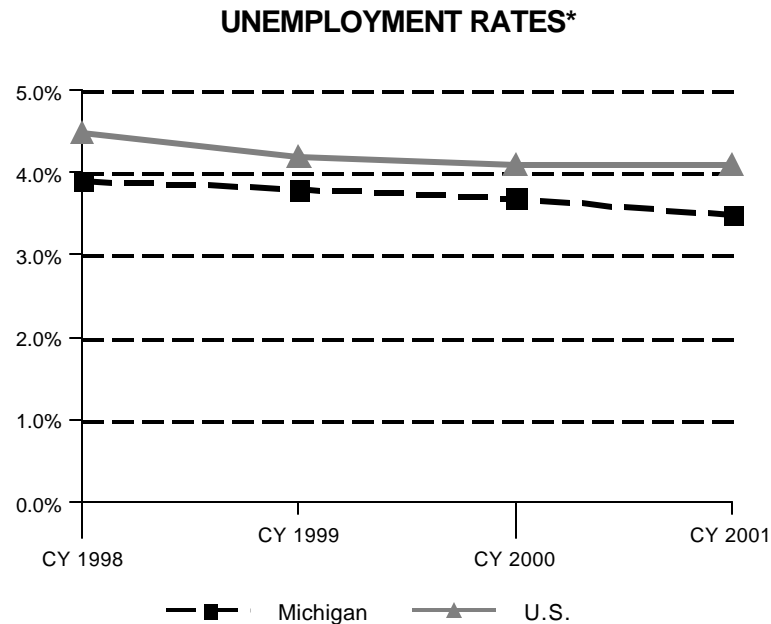
disposable income in CY 1999. This will be followed by growth rates of 3.7% and 4.1% in CY 2000 and CY 2001, respectively.

U Income Growth: Michigan

The Michigan economy continues to expand, and nominal income growth is expected to increase modestly in CY 2000 before dropping back slightly in CY 2001.

Total *state personal income* grew by 4.5% in CY 1999. State personal income growth will increase in CY 2000 to 5.5%, and will then drop to 5.0% in CY 2001.

Figure 7



* Seasonally Adjusted Annual Rate (SAAR)

U Unemployment: U.S.

Non-farm payroll employment increased steadily throughout CY 1998 and the first part of CY 1999, but at a slightly slower pace than the previous year. Between the fourth quarter of 1999 and the first quarter of 2000, non-farm payroll employment increased at an annualized rate of 2.7%. Steady economic growth throughout CY 2000 will allow the economy to continue to create jobs; hence, unemployment rates are expected to remain relatively low.

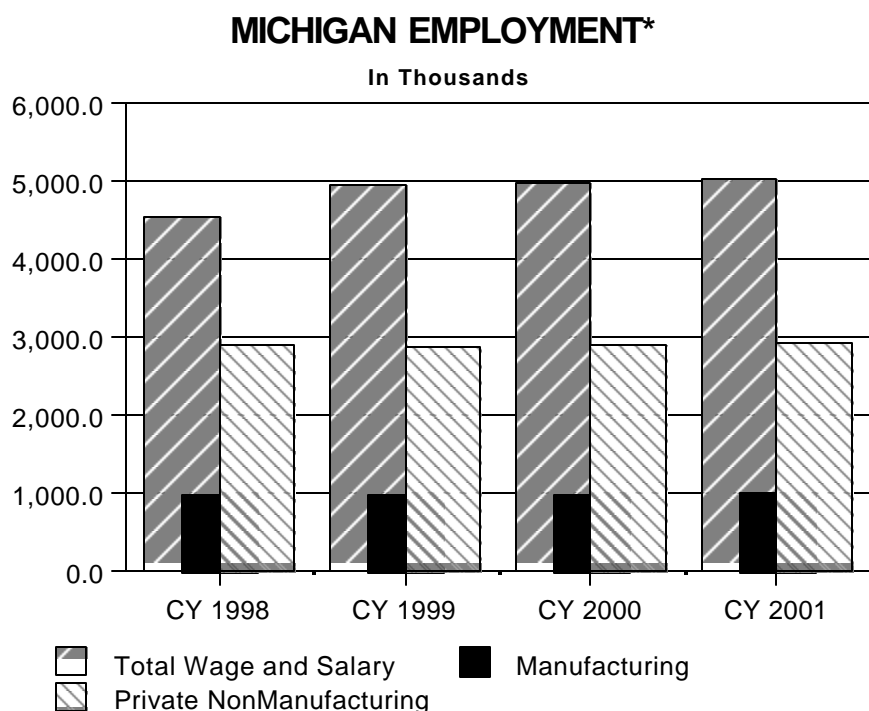
The *U.S. unemployment rate* was 4.2% in CY 1999. Unemployment rates in the U.S. are expected to remain stable at 4.1% in both CY 2000 and CY 2001.

U Unemployment: Michigan

Although the job market is expected to remain somewhat tight, job growth in Michigan is expected to be very slight through CY 2001, and the unemployment rate is expected to decline in CY 2000 and CY 2001. Wage and salary employment in the manufacturing sector is expected to remain flat in CY 2000 and CY 2001.

The *Michigan unemployment rate* in CY 1999 was 3.8%. The unemployment rate is expected to drop to 3.7% in CY 2000 and to 3.5% in CY 2001.

Figure 8



*Composition of Changes (Annual Rate)

U Employment: Michigan

The Michigan economy continued to create jobs in CY 1999, but at a much slower pace relative to CY 1998. However, while manufacturing employment grew in CY 1999, almost all of the employment gains in CY 2000 and CY 2001 are expected to be in private nonmanufacturing.

Total Michigan wage and salary employment increased by 0.7% in CY 1999, and is expected to rise by 1.2% in CY 2000 and 0.9% in CY 2001.

Michigan manufacturing employment rose by 0.8% in CY 1999, but is expected to grow by 0.2% in CY 2000 and decline by 0.2% in CY 2001.

Michigan private nonmanufacturing employment, which increased at a rate of 0.5% in CY 1999, will continue to expand at growth rates of 1.5% in CY 2000 and 1.2% in CY 2001. These increases will once again be fueled by the service sector, as well as by the construction and trade sectors.

Employment in services in Michigan is anticipated to grow by 1.4% in CY 2000 and 1.2% in CY 2001.

Wholesale and retail trade employment in Michigan will grow by 1.4% in CY 2000 and 1.3% in CY 2001.

Construction employment in Michigan will grow by 3.2% in CY 2000 and 2.3% in CY 2001.

Table 2

| ECONOMIC VARIABLES | | | |
|---|---------|---------|---------|
| <u>U.S. FORECAST</u> | | | |
| Variable | CY 1999 | CY 2000 | CY 2001 |
| Rate of Interest, 3-Month Treasury Bill | 4.6% | 6.0% | 6.2% |
| Real GDP Growth | 4.2% | 4.7% | 3.5% |
| Light Vehicle Sales (millions of units) | 16.8 | 17.2 | 16.6 |
| Import Share of Light Vehicle Sales | 14.8% | 16.1% | 15.5% |
| U.S. CPI-U -- Percentage Change | 2.2% | 2.6% | 2.1% |
| U.S. Personal Income Growth | 5.9% | 6.1% | 6.0% |
| Unemployment Rate | 4.2% | 4.1% | 4.1% |
| <u>MICHIGAN FORECAST</u> | | | |
| Variable | CY 1999 | CY 2000 | CY 2001 |
| Detroit CPI-U -- Percentage Change | 2.7% | 2.8% | 2.4% |
| Michigan Personal Income Growth | 4.5% | 5.5% | 5.0% |
| Unemployment Rate | 3.8% | 3.7% | 3.5% |
| Wage and Salary Employment Growth | 0.7% | 1.2% | 0.9% |



RISKS AND UNCERTAINTIES

Prices

Prices are expected to increase slightly in 2000, and then increase at a slower rate in 2001. The thirty-year annual average increase in the U.S. consumer price index was 5.2%; more recent history indicates that over the last seven years the annual average was 2.6%. Two areas of inflation concern are oil prices and labor costs. Oil prices fell to a historically low level in 1998, after which oil prices sharply spiked up in late 1999 to early 2000. Oil prices are expected to decline over the next several months.

Unlike oil, which represents a very small fraction of the economy, labor costs are a major factor. Compensation per hour has been accelerating from an annual rate of 3.7% in 1997 to an average of 5.2% in 1998 and 1999. Given the very tight labor market, which posted a 4.2% unemployment rate in 1999, increasing labor costs are expected. However, strong productivity gains have, so far, prevented higher labor costs from carrying over into higher consumer prices. Labor costs are expected to continue to increase, given the labor market conditions. If productivity gains do not keep pace with

labor costs, then inflation could climb higher than estimated.

Stock Market

Over the last five years, the stock market has increased, on average, 20% per year. This is more than double the long-run average growth. Recently, market fluctuations have been extreme, possibly signaling a decline or flat growth in the future. Included in the forecast is a moderate stock market decline beginning in the second half of 2000, followed by small gains by the end of 2001. Wealth generated by the stock market gains in the last few years has contributed to consumer spending. The future path of the stock market could increase consumer spending and the overall level of economic activity if the strong market gains continue.

Monetary Policy

Built into the forecast is a 50-basis-point increase in the second quarter and an additional 25-basis-point increase in the third quarter of 2000 in both the federal funds rate and the discount rate. Beyond these interest rate changes in 2000, it is expected that the Federal Reserve will take a wait-and-see position. If key prices do

not begin to accelerate or if economic growth returns to a more moderate pace,

then the Federal Reserve will not attempt to slow the economy further.



GF/GP AND SAF REVENUES

This section explains May 2000 House Fiscal Agency revenue estimates for GF/GP and School Aid Fund revenue by major revenue sources. Revenue estimates are based on the economic performance of the national and state key variables. Revenue estimates are reported in **Tables 3 and 4**; the year-end balances for the major funds are included in **Table 5**. In addition, the budget stabilization fund is reported in **Table 6** and the state revenue limit calculation is included in **Tables 7 and 8**.

General Fund/General Purpose Revenue by Source

U Personal Income Tax

Employment is expected to continue to expand in CYs 2000 and 2001, and unemployment rates will continue to decline. In addition, income growth from wages and salaries is expected to post a 6.1% gain in FY 1999-2000 and then slow to 5.6% in FY 2000-01. This will lead to moderately slower growth (as compared to FY 1999-2000) in Michigan personal income and income tax revenues through FY 2000-2001.

Baseline *GF/GP income tax revenues* are expected to increase 7.5%, to \$5,436.4 million, in FY 1999-2000 and 5.6% in FY 2000-01, to \$5,738.6 million. Baseline revenues do not include the impact of indexing the personal exemption or the impact of decreasing the income tax rate

from 4.4% to 4.2% in 2000.

U Sales and Use Taxes

Continued growth in disposable income and sustained low unemployment will combine to increase baseline *sales and use tax revenue* from \$1,001.8 million in FY 1998-99 to \$1,037.8 million in FY 1999-2000 and by 5.6%, to \$1,095.6 million, in FY 2000-01.

U Single Business and Insurance Taxes

All Single Business Tax (SBT) revenues accrue to GF/GP. Net baseline business taxes (SBT plus insurance taxes) were \$2,521.1 million in FY 1998-99. As a result of solid growth in compensation, *baseline business tax revenues* will increase by 3.6%, to \$2,613.0 million, in FY 1999-2000 and by 3.2%, to \$2,696.8 million, in FY 2000-01.

Baseline Single Business Tax revenues alone were \$2,316.0 million in FY 1998-99; they are expected to increase 3.6%, to \$2,400.0 million, in FY 1999-2000 and by 3.2%, to \$2,476.8 million, in FY 2000-01.

Baseline estimates do not include the impact of the SBT rate cut, the apportionment changes, the elimination of the Capital Acquisition Deduction, or the institution of the Investment Tax Credit, all of which will affect FY 1999-2000 and FY 2000-01 revenue collections.

U GF/GP Baseline Tax Revenues

Baseline GF/GP tax revenues totaled \$9,228.6 million in FY 1998-99. *General Fund/General Purpose baseline tax revenues* are expected to increase by 5.7%, to \$9,754.1 million, in FY 1999-2000 and by 4.7%, to \$10,215.0 million, in FY 2000-01.

U Total GF/GP Baseline Revenues

Total baseline GF/GP revenues include baseline tax revenues and non-tax revenues. *Total GF/GP baseline revenues* were \$9,573.8 million in FY 1998-99. General Fund/General Purpose baseline revenues are expected to increase by 4.9%, to \$10,040.1 million, in FY 1999-2000 and by 4.6%, to \$10,503.0 million, in FY 2000-01.

U Actual GF/GP Revenues

Actual GF/GP revenues represent revenues that take into account tax changes and are available for expenditure each year. *Actual GF/GP revenues* are expected to be \$9,656.1 million in FY 1999-2000 and are expected to increase by 1.4%, to \$9,788.0 million, in FY 2000-01.

Table 3

| GF/GP REVENUE ESTIMATES (Millions of Dollars) | | | | | |
|---|--|----------------------------------|--------------------------------|---|------------------|
| | Final Fiscal Year 1998-99 | Fiscal Year 1999-2000 | Fiscal Year 2000-01 | <u>Fiscal Year 2000-01</u> <u>over 1999-2000</u> | |
| | | | | %Change | \$Change |
| Personal Income Taxes | \$5,055.5 | \$5,436.4 | \$5,738.6 | 5.6% | \$302.2 |
| Sales and Use Taxes | 1,001.8 | 1,037.8 | 1,095.6 | 5.6% | 57.8 |
| SBT and Insurance Taxes | 2,521.1 | 2,613.0 | 2,696.8 | 3.2% | 83.8 |
| Other Taxes | 650.2 | 666.9 | 684.0 | 2.6% | 17.1 |
| GF/GP Baseline Tax Revenues | \$9,228.6 | \$9,754.1 | \$10,215.0 | 4.7% | \$460.9 |
| Non-Tax Revenue | 345.2 | 286.0 | 288.0 | 0.7% | 2.0 |
| Total GF/GP Baseline Revenues | \$9,573.8 | \$10,040.1 | 10,503.0 | 4.6% | \$462.9 |
| Adjustments to Baseline | <u>(111.1)</u> | <u>(384.0)</u> | <u>(715.0)</u> | | (\$331.0) |
| Actual GF/GP Revenues | \$9,462.7 | \$9,656.1 | \$9,788.0 | 1.4% | \$131.9 |

School Aid Fund Revenue by Source

U Sales and Use Taxes

Baseline sales tax revenue is expected to increase by 7.2% in FY 1999-2000 and by 4.8% in FY 2000-01; baseline use tax revenue is expected to increase by 6.2% in FY 1999-2000 and by 5.2% in FY 2000-01. Combined *sales and use tax revenue* dedicated to the School Aid Fund (SAF) equaled \$4,739.4 million in FY 1998-99 and will increase by 7.1%, to \$5,076.3 million, in FY 1999-2000 and by 4.9%, to \$5,323.7 million, in FY 2000-01.

U Income Tax

Approximately one quarter of gross income tax revenue is dedicated to the School Aid Fund. Dedicated *income tax revenue* was \$1,848.1 million in FY 1998-99 and is expected to increase by 8.1%, to \$1,997.9 million, in FY 1999-2000 and 5.2%, to \$2,102.2 million, in FY 2000-01.

U State Education Tax

The 6-mill state education tax (SET) is dedicated to the SAF. Revenues from the SET were \$1,273.5 million in FY 1998-99. *State Education Tax revenues* are expected to increase 8.1%, to \$1,376.6 million, in FY 1999-2000 and 5.5%, to \$1,452.3 million, in FY 2000-01.

U Lottery Transfers

Lottery revenues contributed \$621.1 million to the SAF in FY 1998-99. *Lottery revenues* to the SAF are projected to decline to \$616.0 million in FY 1999-2000 and then increase slightly to \$620.0 million in FY 2000-01.

Baseline revenue estimates do not include the impact of Detroit Casinos. The casino/gaming tax is expected to be \$45.7 million in FY 1999-2000 and \$78.3 million

in FY 2000-01. These amounts appear in the adjustments to baseline revenues.

U Tobacco Taxes

Approximately 64.0% of gross tobacco tax revenue is dedicated to the School Aid Fund. The School Aid Fund received approximately \$394.4 million from tobacco taxes in FY 1998-99. The demand for tobacco products is expected to decline slowly over the duration of the forecast. Total baseline *tobacco tax revenues* are expected to decrease to \$386.6 million in FY 1999-2000 and to \$380.9 million in FY 2000-01.

U Real Estate Transfer Tax

Real estate transfer tax revenues are dedicated to the School Aid Fund. The *transfer tax* contributed \$261.7 million to the SAF in FY 1998-99 and is expected to contribute \$273.2 million to the SAF in FY 1999-2000 and \$270.0 million in FY 2000-01.

U Total SAF Baseline Revenues

Total SAF baseline revenues were \$9,314.4 million in FY 1998-99. *School Aid Fund baseline revenues* are expected to increase 6.6%, to \$9,925.2 million, in FY 1999-2000 and 4.2%, to \$10,341.6 million, in FY 2000-01.

U Actual SAF Revenues

Actual SAF revenues represent own-source revenues available for expenditure each year, excluding prior year-end balances, and GF/GP transfers to SAF. *Actual SAF revenues* were \$9,309.9 million in FY 1998-99 and are expected to increase by 6.7%, to \$9,936.9 million in FY 1999-2000 and by 4.3%, to \$10,365.3 million, in FY 2000-01.

Table 4

| SCHOOL AID FUND REVENUE ESTIMATES (Millions of Dollars) | | | | | |
|--|---------------------------------|--------------------------|------------------------|---|----------------|
| Revenues | Final Fiscal Year 1998-99 | Fiscal Year 1999-2000 | Fiscal Year 2000-01 | <u>2000-01 over</u> <u>1999-2000</u> % Change | \$ Change |
| Sales and Use Tax | \$4,739.4 | \$5,076.3 | \$5,323.7 | 4.9% | 247.4 |
| Income Tax Earmark | 1,848.1 | 1,997.9 | 2,102.2 | 5.2% | 104.2 |
| State Education Tax | 1,273.5 | 1,376.6 | 1,452.3 | 5.5% | 75.7 |
| Lottery Transfers | 621.1 | 616.0 | 620.0 | 0.6% | 4.0 |
| Tobacco Taxes | 394.4 | 386.6 | 380.9 | -1.5% | (5.7) |
| Real Estate Transfer Tax | 261.7 | 273.2 | 270.0 | -1.2% | (3.2) |
| Other Taxes | 176.1 | 198.6 | 192.6 | -3.0% | (6.0) |
| Baseline SAF Revenues | \$9,314.4 | \$9,925.2 | \$10,341.6 | 4.2% | \$416.4 |
| Adjustments to Baseline | (4.5) | 11.7 | 23.7 | | |
| Actual SAF Revenues (less GF/GP Transfer) | \$9,309.9 | \$9,936.9 | \$10,365.3 | 4.3% | \$428.4 |

NOTE: Numbers may not add due to rounding.

HFA Estimates of Year-End Balances

Table 5 reports House Fiscal Agency estimates of year-end balances for GF/GP, the SAF, and the BSF.

Fiscal Year 1999-2000 estimates are based on year-to-date appropriations and HFA revenue estimates. Final FY 1997-98 and FY 1998-99 figures are included.

Budget Stabilization Fund estimates are based on current balance estimates provided by the Michigan Department of Treasury and HFA estimates of future deposits and interest earned.

School Aid Fund revenues are restricted; hence, any year-end balance is carried forward to the subsequent year.

Table 5

| YEAR-END BALANCE ESTIMATES (Millions of Dollars) | | | |
|---|---------------------------------|---------------------------------|---------------------------------------|
| | Final Fiscal Year 1997-98 | Final Fiscal Year 1998-99 | Estimated Fiscal Year 1999-2000 |
| General Fund/General Purpose | \$55.2 | \$0.0 ¹ | \$100.4 ² |
| School Aid Fund | 274.3 | 572.8 | 989.2 |
| Budget Stabilization Fund | 1,000.5 | 1,222.5 | 1,305.6 |

¹ The FY 1998-99 GF/GP year-end balance of \$189.2 million was transferred to the Budget Stabilization Fund.

² The estimated FY 1999-2000 GF/GP year-end balance assumes passage of the \$239.2 million supplemental appropriation currently before the House (SB 968 S-1) and the \$100.0 million governor's recommendation for Build Michigan III.

Budget Stabilization Fund
Year-End Balances

Table 6 and Figure 9 show a history of the BSF balance. Table 6 shows deposits, withdrawals, and interest earnings from FY 1989-90 through FY 1998-99. It also includes HFA estimates

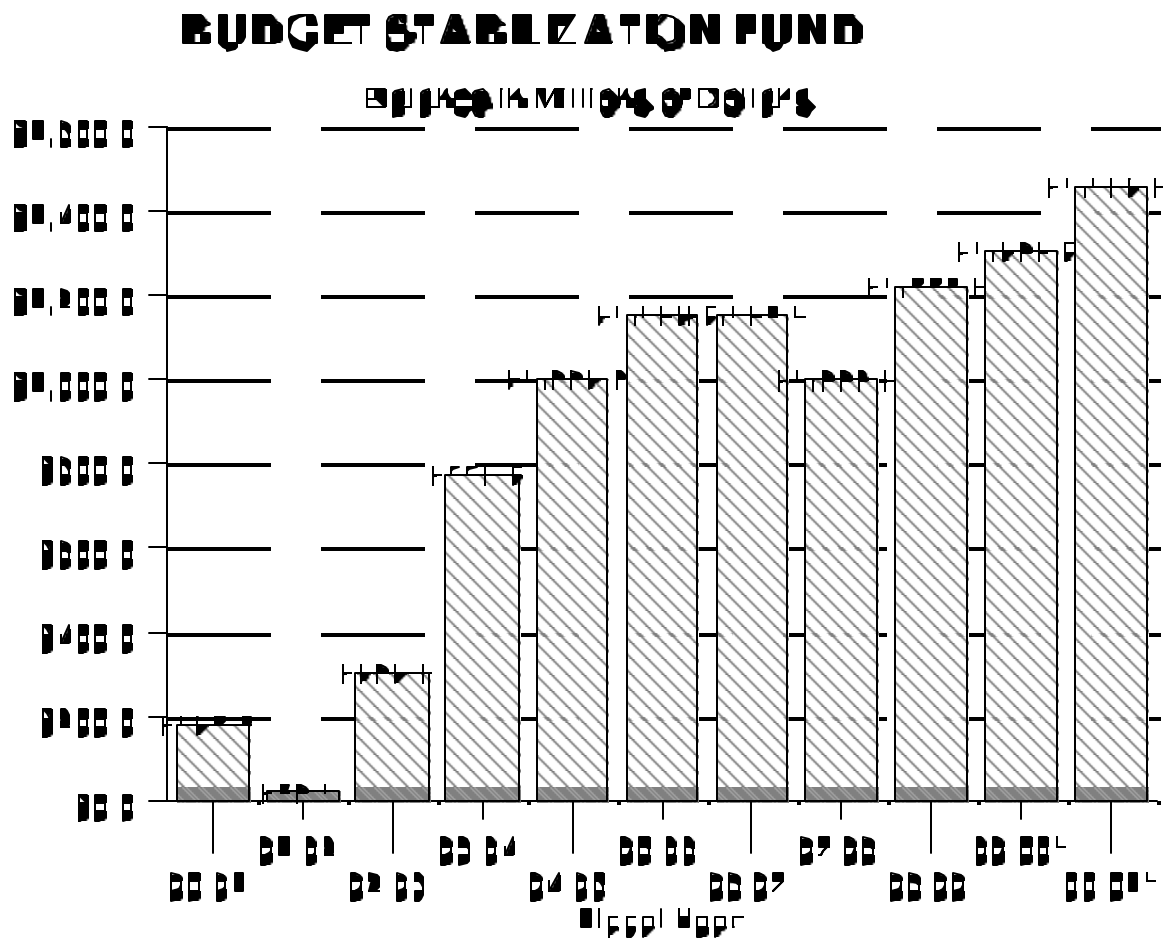
of deposits, expected interest earnings, and year-end balances for FY 1999-2000 and 2000-01.

A complete list of BSF historical data is available from the HFA upon request.

Table 6

| BUDGET STABILIZATION FUND (Millions of Dollars) | | | | |
|--|----------|-------------|-----------------|---------|
| Fiscal Year | Deposits | Withdrawals | Interest Earned | Balance |
| 1989-90 | \$0.0 | \$69.9 | \$35.8 | \$385.1 |
| 1990-91 | 0.0 | 230.0 | 27.1 | 182.2 |
| 1991-92 | 0.0 | 170.1 | 8.1 | 20.1 |
| 1992-93 | 282.6 | 0.0 | 0.8 | 303.5 |
| 1993-94 | 460.2 | 0.0 | 11.9 | 775.6 |
| 1994-95 | 260.1 | 90.4 | 57.7 | 1,003.0 |
| 1995-96 | 91.3 | 0.0 | 59.2 | 1,153.6 |
| 1996-97 | 0.0 | 69.0 | 67.8 | 1,152.4 |
| 1997-98 | 0.0 | 212.0 | 60.1 | 1,000.5 |
| 1998-99 | 244.4 | 73.7 | 51.2 | 1,222.5 |
| 1999-2000* | 37.1 | 32.0 | 78.0 | 1,305.6 |
| 2000-01* | 93.9 | 32.0 | 91.0 | 1,458.5 |
| * Estimates | | | | |
| NOTE: Numbers may not add due to rounding. | | | | |

Figure 9



*Estimates

**Compliance with the State
Revenue Limit**

Table 7 reports HFA estimates of the state revenue limit provided for in Article IX, Section 26, *Constitution of the State of Michigan*, and estimates of total state revenue collections subject to the state revenue limit. As provided

for in the *Constitution*, the revenue limit is calculated as 9.49% of total state personal income in the previous full calendar year prior to the fiscal year in which the revenues are measured, as estimated by the Bureau of Economic Analysis, United States Department of Commerce.

Table 7

| COMPLIANCE WITH THE STATE REVENUE LIMIT (Millions of Dollars) | | | | |
|--|---------------------------------|---------------------------------|--------------------------|------------------------|
| Revenue Limit Calculations | Final Fiscal Year 1997-98 | Final Fiscal Year 1998-99 | Fiscal Year 1999-2000 | Fiscal Year 2000-01 |
| Personal Income | | | | |
| Calendar Year | CY 1996 | CY 1997 | CY 1998 | CY 1999 |
| Amount | \$239,330 | \$244,329 | \$255,039 | \$266,531 |
| X Limit Ratio | 9.49% | 9.49% | 9.49% | 9.49% |
| State Revenue Limit | \$22,712.4 | \$23,186.8 | \$24,203.2 | \$25,293.8 |
| Total Revenues Subject to Revenue Limit | 22,072.3 | 23,208.5 | 24,162.0 | 24,859.3 |
| Amount Under (Over) State Revenue Limit | \$640.1 | (\$21.7) | \$41.2 | \$434.5 |

**Implications of Exceeding
the State Revenue Limit**

Article IX, Section 26, *Constitution of the State of Michigan*, provides that:

. . . For any fiscal year in the event that Total State Revenues exceed the limit established in this section by 1% or more, the excess revenues shall be refunded pro rata based on the liability reported on the Michigan income tax and single business tax (or its successor tax or taxes) annual returns filed following the close of such fiscal year. If the excess is less than 1%, this excess may be transferred to the State Budget Stabilization Fund.

. . .

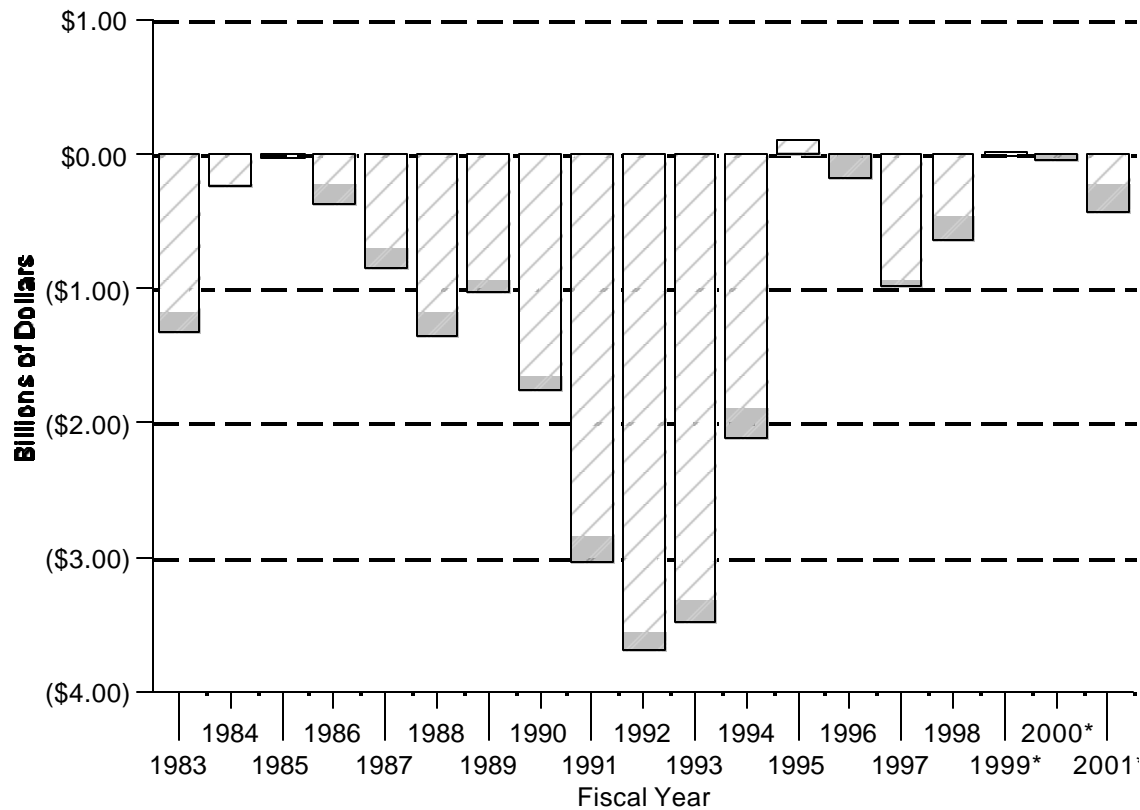
Furthermore, the state is prohibited from spending any current-year revenue in excess of the limit established in Section 26 by Article IX, Section 28.

Figure 10 and **Table 8** provide historical information on Michigan's state revenue limit.

Figure 10

CONSTITUTIONAL REVENUE LIMIT

Amount Under or Over Limit



*HFA estimates

Table 8

| CONSTITUTIONAL REVENUE LIMIT Amount (Under) or Over Limit in Billions of Dollars | | | |
|---|---------------------------|-------------|---------------------------|
| Fiscal Year | Amount (Under) or Over | Fiscal Year | Amount (Under) or Over |
| 1980 | (\$0.53) | 1991 | (\$3.04) |
| 1981 | (\$1.17) | 1992 | (\$3.69) |
| 1982 | (\$1.41) | 1993 | (\$3.48) |
| 1983 | (\$1.32) | 1994 | (\$2.11) |
| 1984 | (\$0.24) | 1995 | \$0.11 |
| 1985 | (\$0.01) | 1996 | (\$0.18) |
| 1986 | (\$0.37) | 1997 | (\$0.98) |
| 1987 | (\$0.84) | 1998 | (\$0.64) |
| 1988 | (\$1.35) | 1999 | \$0.02 |
| 1989 | (\$1.03) | 2000* | (\$0.04) |
| 1990 | (\$1.76) | 2001* | (\$0.43) |

*HFA Estimates



Additional copies of this report can be obtained from:

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